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C O N F I D E N T I A L SECTION 01 OF 02 ROME 001445

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STATE FOR S/CT
DEPT PLEASE PASS TO OPIC AND EXIM BANK

E.O. 12958: DECL: 11/20/2018
TAGS: PREL KNNP EFIN ETRD IT IR
SUBJECT: ITALY REDUCES IRAN EXPORT CREDIT AND INSURANCE

Classified By: Deputy Chief of Mission Elizabeth L. Dibble
for reasons 1.4 (b) and (d).

¶1. (C) Summary: SACE, the Italian government's export credit agency and foreign investment promotion and insurance arm, has over the last 12 months substantially reduced its exposure to Iran because of uncertainty surrounding future sanctions. SACE's Chief Economist told post that this reduction is driven by commercial and credit realities; Italian political leaders have not attempted to influence SACE's operations. SACE's export credit and investment insurance exposure to Iran, currently around 1.5 billion euros, may disappear by 2012. Lacking SACE financing, Italian exporters are shifting attention to other markets, including Brazil. While we would prefer a more principled motive for SACE cutting Iran off, the end result is desirable nonetheless. End Summary.

2.Q(C) On 19 November, SACE Chief Economist Emanuele Baldacci told Econoffs that SACE had reduced its export credit and investment insurance exposure to Iran from 3 billion euros to 1.5 billion euros and that he expects this exposure to decrease by approximately 250 million euros per year over the next few years. Of this amount, approximately 500 million euros are for export credits. Insurance "exposure" of one billion euros will decrease as political risk policies expire and SACE declines to renew them. SACE is the Italian equivalent of OPIC and the ExIm bank, providing export insurance, some political risk insurance and hedges against interest rate risk for Italian companies doing business in emerging markets, including Iran. Since January of 2007 SACE has had an informal policy of not writing new insurance policies or extending new trade credits to Iran due to sanctions uncertainty, although Iran remains officially "open" to SACE activity, albeit with poor sovereign and political risk ratings. According to Baldacci SACE has chosen not to formalize this policy (by 'closing' Iran, for example) because doing so might adversely affect the likelihood of SACE's clients being repaid by Iranian entities. Baldacci said that Italy-Iran trade flows were down as a result of SACE's policy and that by the end of 2012 SACE's exposure to Iran could disappear altogether.

3.Q(C) Italian banks and exporters have given up seeking new credits from SACE for trade with Iran, Baldacci said, although Iranian representatives have continued to make ocassional inquires for new business from SACE. SACE had politely rebuffed these entreaties, according to Baldacci. Italy's goal over the coming five years with respect to Iran is to be repaid outstanding credits without extending new ones and to reduce its insurance exposure. All SACE exposure is in euros, not dollars. Baldacci indicated that American sanctions on Iranian banks had not

prevented the Iranians from paying their obligations on SACE-guaranteed credits. Approximately two thirds of Italian investment insurance exposure to Iran is in the oil and gas industry. Baldacci said that Iranian elections in the spring will be the next milestone prompting SACE officials to calibrate its policy towards Iran.

4.Q(C) Some Italian exporters have complained that German competitors continue to receive strong support from SACE's German counterpart for investments in Iran, while SACE has been moving in the opposite direction, thereby putting Italian companies at a disadvantage. (Comment: This does not necessarily reflect a change in GOI policy, as Baldacci said it was rare for the GOI to intrude in operational matters, and even at the strategic level the GOI typically takes a hands-off approach to SACE. End comment.) To make up for lost markets in Iran, Italian firms have shifted their efforts to new areas. Baldacci noted that Latin America and especially Brazil have become attractive to Italian exporters.

5.Q(C) SACE's total worldwide exposure is 30 billion euros, while its current capital cushion is 7 billion euros. The agency typically makes a few hundred million euros in profit per year, though its loss rate is starting to climb.

¶6. (C) Comment: While we welcome the decline in SACE's exposure in Iran, the Italian position on Iran export credits is not entirely satisfactory. If SACE's current posture toward Iran is governed exclusively by credit risk, there's nothing to stop it from resuming support for Iran

in the event credit and political risk conditions improve, irrespective of Iran's ongoing nuclear ambitions and support for terrorism. Moreover, Iran has demonstrated in the past a talent for toning down its combative rhetoric when it suited more immediate objectives such as resuming the flow of trade and technology the regime needs. We would prefer that SACE cease support for Iran on political grounds as well, but we are pleased that they are currently reducing their operations in that country. End comment.

DIBBLE